

STATE OF MICHIGAN
COURT OF APPEALS

ROYAL OAK SCHOOL DISTRICT,

Plaintiff-Appellant,

v

MASB-SEG PROPERTY AND CASUALTY
PPL, INC.,

Defendant-Appellee.

UNPUBLISHED
September 16, 2003

No. 235260
Oakland Circuit Court
LC No. 99-019088-CK

Before: Wilder, P.J., and Griffin and Gage, JJ.

PER CURIAM.

This appeal involves a dispute over insurance coverage. Plaintiff claimed damages under its policy resulting from alleged Y2K problems.¹ Defendant denied coverage based on an exclusion in the policy. The trial court granted summary disposition to defendant. Plaintiff now appeals as of right. Plaintiff also appeals the trial court order denying its motion for class certification. We affirm.

Defendant first issued plaintiff insurance coverage effective July 1, 1996. Thereafter, the policy was renewed annually, effective every July 1. On August 16, 1999, defendant sent plaintiff an insurance renewal package, which contained the renewal certificates and an invoice for payment for the policy term effective July 1, 1999. In the package, defendant also included a notice of exclusion, which excluded coverage under the policy for any Y2K problems.²

¹ As most well know, Y2K stands for Year 2000. Some people anticipated that because of the way computers were programmed, some computer programs would experience problems interpreting the year 2000.

² The property coverage exclusion states in relevant part:

A. This policy does not insure against loss or damage consisting of or caused directly or indirectly by any of the following. Such loss is excluded regardless of any other cause or event that contributes concurrently or in any sequence to the loss except as provided in B.

(continued...)

Thereafter, without disputing the policy exclusion or any other aspect of coverage, plaintiff paid its premium in September 1999. On October 28, 1999, plaintiff notified defendant of its claim for “year 2000 remediation expenses and/or damages” under the policy. Defendant refused coverage.

On November 18, 1999, plaintiff brought suit for breach of the insurance contract issued by defendant. According to plaintiff, certain property covered under the insurance policy was impacted by Y2K problems. This property included personal computers, embedded chips, HVAC control systems, and telephone systems. To address these problems, plaintiff developed a program to identify all information technology systems, facility systems, and other types of

(...continued)

1. The failure, malfunction or inadequacy or the inability to use or have access to:

a. Any of the following, whether belonging to the Insured or to others:

(1) computer hardware, including microprocessors;

(2) computer application software;

(3) computer operating systems and related software;

(4) computer networks;

(5) microprocessors (computer chips) not part of any computer system;

(6) any other computerized or electronic equipment or components; or

(b) Any other products or services that directly or indirectly use or rely upon, in any manner, any of the items listed in paragraph 1.a. of this endorsement;

due to the inability of those products or services described in paragraph 1.a. and 1.b. to correctly recognize, distinguish, interpret or accept on or more dates or times.

* * *

C. This policy does not insure against any preventive or remedial costs to repair or modify any items in A.1.a. and b. above to correct any actual or potential deficiencies or change any features of logic or operation.

D. This policy does not insure against any expense incurred by the insured or others in the defense, safeguarding, protecting or recovering of property whether before or after loss due to any actual or potential loss excluded in paragraph A. above.

covered property impacted by Y2K programming errors and to remediate, renovate, or replace the impacted property. According to plaintiff, defendant failed to acknowledge coverage under the policy and attempted to invoke the “Y2K Exclusion.” Plaintiff brought suit for breach of contract on behalf of itself and all others similarly situated.

On July 14, 2000, plaintiff moved, pursuant to MCR 3.501, for class certification. At a hearing on this motion, the trial court ruled against class certification, stating

My reaction is that this is a claim of the Royal Oak School District, and does not rise in my opinion to the level of a class action, as no other class actions have been filed. I’ve never known anybody, if they felt it necessary at the school district that they were being harassed or harmed, that they wouldn’t pursue their legal remedies in connection with it.

In the event that more actions are filed and they want to compile their – join them together and perhaps a class action then, okay, but now, no. Okay? I’m not satisfied with the necessity.

The trial court entered an order denying plaintiff’s motion for class certification on October 31, 2000.

Both parties thereafter moved for summary disposition. The trial court granted defendant’s motion for summary disposition and denied plaintiff’s motion, finding that plaintiff assented to the change, or exclusion, in the policy by paying the premium without objection.

Plaintiff now contends that the trial court erred in granting defendant’s motion for summary disposition because the Y2K exclusion was unilaterally issued in the middle of the policy, without plaintiff’s consent and without giving consideration to plaintiff. We disagree.

This Court reviews the grant of summary disposition de novo to determine if the moving party is entitled to judgment as a matter of law. *Maiden v Rozwood*, 461 Mich 109, 118; 597 NW2d 817 (1999). In evaluating a motion brought under MCR 2.116(C)(10), the trial court considers affidavits, pleadings, depositions, admissions, and other evidence submitted by the parties in a light most favorable to the party opposing the motion. *Id.*

The law in Michigan places a duty on the insured to read an insurance policy and raise any questions concerning coverage within a reasonable time after the issuance of the policy. *Parmet Homes Inc v Republic Ins Co*, 111 Mich App 140, 145; 314 NW2d 453 (1981), citing *House v Billman*, 340 Mich 621; 66 NW2d 213 (1954); *Russel v State Farm Mut Automobile Ins Co*, 47 Mich App 677; 209 NW2d 815 (1973); see also *American Cas Co of Reading, Pennsylvania v Rahn*, 854 F Supp 492, 502 (WD Mich, 1994). This rule does not apply, however, when a renewal policy is issued without calling to the insured’s attention a reduction in coverage, as the insurer in those circumstances is bound by the greater coverage in the earlier policy. *Id.* In this regard, this Court has stated:

“While the renewal of an insurance policy constitutes a separate contract to be governed by general contract principles, it is the general rule that an insurance company is bound by the greater coverage in an earlier policy where the

renewal contract is issued without calling to the insured's attention a reduction in policy coverage.” [*Industro Motive Corp v Morris Agency, Inc*, 76 Mich App 390, 395-396; 256 NW2d 607 (1977), quoting *Gov't Employees Ins Co v United States*, 400 F2d 172, 174-175 (CA 10, 1968).]

By way of example on the law regarding the renewal of an insurance policy, we look to the court's analysis in *American Cas Co, supra*. While we acknowledge that the court's analysis is not binding, we find it instructive. In that case, American Casualty Company (ACC) sought a declaratory judgment that it was not required to provide coverage under the director and officer liability policies it issued to Peoples Savings Association (PSA). *Id.* at 494. The first policy was effective from June 30, 1981, until June 30, 1984. In June 1984, PSA requested the renewal of the policy. Unlike the 1981 policy, the 1984 policy included a “regulatory exclusion” that excluded coverage for claims by or on behalf of regulatory agencies, such as the FDIC. *Id.* at 494-495.

PSA became aware of the exclusion and the resulting coverage sometime in 1984. *Id.* at 495. PSA's president unsuccessfully attempted, in the spring of 1985, to have ACC remove the exclusion. PSA thereafter entered into a supervisory agreement with the Federal Home Loan Bank Board (FHLBB) on May 27, 1987, prior to the expiration of the 1984 policy. This agreement stated that FHLBB was of the opinion that PSA violated certain statutes and regulations and engaged in unsafe or unsound business practices. *Id.*

PSA argued that ACC committed wrongful conduct in the manner in which it secured the 1984 policy “renewal,” and sought two possible remedies: that they be allowed to purchase discovery coverage or that the policy be reformed to exclude the Regulatory Exclusion. *Id.* at 501. The court found that at the time the policy was renewed, no mention was made by ACC that coverage would be reduced significantly or that the Regulatory Exclusion Endorsement was going to be attached. *Id.* In addition, when the actual policy was sent to PSA in early August 1984, there was no notification that the “renewal” was not of the identical coverage. *Id.* Nonetheless, the court then continued:

I believe that once PSA had notice of the policy changes, it was incumbent upon it to air its concerns within a reasonable time. Further, its failure to cancel the policy, once it learned of the Regulatory Exclusion and was unsuccessful at obtaining its removal from the policy, constitutes an acceptance of the terms as they existed in the 1984 policy. This conclusion is supported by the fact that PSA actually renewed the 1984 policy in 1987, including the Regulatory Exclusion.

Whether the acceptance following notice is considered a “renewal” as of that time or merely assent to the terms of a new insurance contract is an unimportant label. The bottom line is that PSA could have sought alternate coverage and cancelled the ACC policy. It did not do so. It instead sought, unsuccessfully, to have the Regulatory Exclusion removed. It cannot now seek an equitable remedy from this Court to obtain what it was unable to bargain for: liability coverage without the Regulatory Exclusion. [*Id.* at 503.]

In the present case, defendant's agent sent a letter regarding MASB-SEG policy 63040 to plaintiff's executive director of business affairs on August 16, 1999. This letter stated:

Enclosed is the renewal of the above-captioned policy, including Equipment Breakdown (Boiler) insurance (applicable), as well as an invoice for payment. This packet also contains Continuation Certificates and Endorsements, which should be placed over the expiring Declarations in your policy booklet, and a new Certificate of Insurance of your vehicles

In conformance to insurance industry practices, as well as the requirements of the Pool's re-insurer, an exclusion for Year 2000-related developments is being implemented. A copy is included in these materials. Basically, this excludes coverage for computer failure related to Year 2000 causes, however, the policy provides coverage for consequential damage, except for mechanical damage. Districts that carry the Equipment Breakdown policy are covered for mechanical damage. The exclusion takes effect with the new policy year, July 1, 1999. Each district should proactively address and remedy its Year 2000 vulnerabilities. Please refer to the enclosed "Safety Focus" newsletter for tips on identifying these vulnerabilities and developing an action plan to address them.

As you review your invoice, you'll notice that rates remain unchanged. Any variance in premium reflects changes in your exposures, such as increased building and equipment values

Unlike the "renewal" in *American Cas Co, supra*, the August 16, 1999 letter sent to plaintiff regarding the "renewal" specifically informed plaintiff that an exclusion for Year 2000-related developments was being implemented. Therefore, plaintiff had notice of the policy changes. Because plaintiff was properly notified of the change, plaintiff was obligated to read the insurance policy and raise questions concerning coverage within a reasonable time after the issuance of the policy. *Parment Homes, supra* at 145.³ Plaintiff briefly mentions on appeal that it did object to the exclusion and ask that it be rescinded. Plaintiff further states that defendant refused to respond and that plaintiff had to pay its premium for the \$150 million in insurance coverage. However, like the court's reasoning in *American Casualty Co, supra*, plaintiff's unsuccessful attempt to remove the exclusion from the policy, its failure to challenge the issue further, and its subsequent payment of the policy premium without dispute, constitute an acceptance of the policy effective July 1, 1999.

Plaintiff contends that defendant's exclusion constituted a prohibited mid-term policy change. We disagree. While we acknowledge that had defendant sent plaintiff the renewal and exclusion information before July 1, 1999, as opposed to after, there likely would be no dispute, the fact that the exclusion was sent after July 1 does not change our analysis. Plaintiff has provided no basis to find that the change was an improper mid-term policy change. Instead, defendant sent plaintiff the renewal and exclusion information effective July 1, and plaintiff thereafter paid the premium without dispute. At the time plaintiff received the renewal and exclusion information, plaintiff had not paid the premium for the July 1, 1999 to July 1, 2000

³ We note that whether the acceptance after notice is considered a renewal of the policy, or rather an assent to a new contract, is of no import as our analysis in this case remains the same in either instance.

period, and thus, had not agreed to the coverage. Plaintiff was given adequate notice of the change in the policy and, plaintiff's payment of the policy premium without challenging the policy change constitutes acceptance of the change effective July 1, 1999. Therefore, we conclude that the trial court did not err in granting defendant's motion for summary disposition.

Plaintiff next contends that the trial court erred in ruling that its losses were not "fortuitous." As noted above, the trial court granted summary disposition in favor of defendant on the basis that plaintiff assented to the change in the policy by paying the premium without objection. The trial court acknowledged that the parties raised numerous other arguments, including defendant's argument that there was no unexpected loss on the part of the plaintiff. The trial court agreed with defendant and stated, "[t]here were warnings about the potential problems of Y2K for years before January 1, 2000." The trial court, however, emphasized that the argument regarding the exclusionary provision was dispositive on the motion. Because the trial court did not err in granting defendant's motion for summary disposition on the basis that plaintiff assented to the change in the policy and because the issue of whether plaintiff's losses were "fortuitous" was not dispositive of the motion, we decline to address this argument.

Plaintiff next contends that the trial court erred in denying its motion for summary disposition where the undisputed facts show that plaintiff sustained a "direct physical loss" resulting from an external cause. We disagree.

As noted, the exclusion contained the following language:

A. This policy does not insure against loss or damage consisting of or caused directly or indirectly by any of the following. Such loss is excluded regardless of any other cause or event that contributes concurrently or in any sequence to the loss except as provided in B.

1. The failure, malfunction or inadequacy or the inability to use or have access to:

a. Any of the following, whether belonging to the Insured or to others:

(1) computer hardware, including microprocessors;

(2) computer application software; . . .

This Court applies general rules of construction when interpreting insurance policies. *South Macomb Disposal Auth v American Ins Co (On Remand)*, 225 Mich App 635, 653; 572 NW2d 686 (1997). When interpreting a policy,

A court determines whether the policy is clear and unambiguous on its face. *Upjohn Co v New Hampshire Ins Co*, 438 Mich 197, 206; 476 NW2d 392 (1991). Courts may not create ambiguities where none exist, but must construe ambiguous policy language in the insured's favor. *Fire Ins Exchange v Diehl*, 450 Mich 678, 687; 545 NW2d 602 (1996) [overruled in part sub nom *In re Estate of Wilkie*, ___ Mich ___ (2003)]. Clear and unambiguous language may not be rewritten under the guise of interpretation; contract terms must be enforced as written, and

unambiguous terms must be construed according to their plain and commonly understood meaning. *Upjohn, supra* at 207; *Auto Club Ins Ass'n v Lozanis*, 215 Mich App 415, 419; 546 NW2d 648 (1996). Additionally, an insurance contract should be viewed as a whole and read to give meaning to all its terms. *Fresard v Michigan Millers Mut Ins Co*, 414 Mich 686, 694; 327 NW2d 286 (1982). Conflicts between clauses should be harmonized, and a contract should not be interpreted so as to render it unreasonable. *Id.* [*South Macomb Disposal Auth, supra* at 653.]

“Exclusionary clauses are strictly construed in the insured’s favor.” *South Macomb Disposal Auth, supra* at 653, citing *Auto-Owners Ins Co v Churchman*, 440 Mich 560, 567; 489 NW2d 431 (1992). A clear and specific exclusion must be given effect. *Id.*, citing *Churchman, supra*. “If any exclusion in an insurance policy applies to a claimant’s particular claims, coverage is lost.” *Id.* at 654, citing *Churchman, supra*.

Based on the language of the exclusion, to which plaintiff assented, we find plaintiff’s claim for Y2K expenses and damages was barred. Therefore, the trial court did not err in denying plaintiff’s motion for summary disposition.

Plaintiff also contends that the trial court erred in denying its motion for summary disposition where the undisputed facts showed that its remediation expenses were incurred pursuant to the policy’s “protection of policy clause.” Again, we disagree.

Paragraph 18 under the “General Conditions” section of the policy states

Protective Safeguards. If as a condition of this insurance that the insured shall maintain so far as within his control such protective safeguards as are set forth by endorsement hereto

Failure to maintain such protective safeguards shall suspend this insurance only as respects the location or situation affected for the time of such discontinuance.

In addition, the Data Processing Extra Expense Form states the following:

1. **Subject of Insurance and Perils Insured.** This coverage insures against necessary Extra Expense, as defined, incurred by **you** in order to continue as nearly as practicable the normal operation of business as a direct result of the all risks of direct physical loss or damage from any external cause (except as excluded) to the following property owned, leased [sic] rented or under **your** control:

- a. Data Processing systems, computer systems or other electronic control equipment including component parts;
- b. Active data processing media meaning all forms of converted data and/or program and/or instruction vehicles employed in **your** data processing or production operation except the following:

None

This provision states that it is subject to any exclusions. Because we conclude that plaintiff assented to the provision that excluded coverage for loss or damage caused by the failure or malfunction of any computer hardware or computer application software, it follows that the trial court did not err in denying plaintiff's motion for summary disposition because such reimbursement was clearly excluded.

Finally, plaintiff contends the trial court erred in denying its motion for class certification. "This Court reviews a trial court's ruling on class certification under the clearly erroneous standard." *Zine v Chrysler Corp*, 236 Mich App 261, 270; 600 NW2d 384 (1999), citing *Mooahesh v Dep't of Treasury*, 195 Mich App 551, 556; 492 NW2d 246 (1992).

MCR 3.501(A) sets forth the requirements for establishing the need for class certification

(1) One or more members of a class may sue or be sued as representative parties on behalf of all members in a class action only if:

(a) the class is so numerous that joinder of all member is impracticable;

(b) there are questions of law or fact common to the members of the class that predominate over questions affecting only individual members;

(c) the claims or defenses of the representative parties are typical of the claims or defenses of the class;

(d) the representative parties will fairly and adequately assert and protect the interests of the class; and

(e) the maintenance of the action as a class action will be superior to other available methods of adjudication in promoting the convenient administration of justice.

The plaintiff has the burden of proving that the action satisfies every one of the above factors. *A & M Supply Co v Microsoft Corp*, 252 Mich App 580, 597-598; 654 NW2d 572 (2002). "[A] case cannot proceed as a class action when it satisfies only some, or even most, of these factors." *Id.* at 597. "There being little Michigan case law construing MCR 3.501, it is appropriate to consider federal cases construing the similar federal court rule (FR Civ P 23) for guidance." *Zine, supra*, 287 (citing *Brenner v Marathon Oil Co*, 222 Mich App 128, 133; 565 NW2d 1 (1997)).

With regard to the requirement of numerosity, this Court has determined that there is no particular minimum number of members necessary to meet the requirement and the exact number of members need not be known as long as general knowledge and common sense indicate that the class is large. *Zine, supra* at 288 (citations omitted). In *Zine*, this Court stated:

Because the court cannot determine if joinder of the class members would be impracticable unless it knows the approximate number of members, the plaintiff

must adequately define the class so potential members can be identified and must present some evidence of the number of class members or otherwise establish by reasonable estimate the number of class members. [*Zine, supra*, 288 (citations omitted).]

In this case, in support of the motion for class certification, plaintiff argued that because it proposed a class of 400 Michigan school districts that spent money protecting their property for Y2K problems, the class is so numerous that joinder of all its members would be impracticable. Plaintiff further argued that “Plaintiffs [sic] counsel is confident that at least 300 of the 400 Michigan school districts that Defendant insures belong to the putative class if for no other reason than that Defendant has acknowledged sending **retroactive** Y2K exclusions to that many districts.” In support of its motion for class certification, plaintiff offered as evidence data from a survey defendant conducted concerning Y2K issues. Plaintiff argued that defendant’s own data from the survey showed the potential for millions of dollars in Y2K-related claims from members who were already planning and budgeting to deal with the problem.

The survey conducted by defendant asked questions such as:

- (1) Does your school district have a written plan to address Year 2000 issues?
- (2) Has your school district identified and prioritized operating systems and/or applications that *are* Year 2000 compliant?
- (3) Has your school district calculated the financial impact of failure to bring its technology into Year 2000 compliance?
- (4) Have you budgeted resources (such as hardware, people and dollars) with which to address Year 2000 issues? [Appendix A.]

One hundred and thirty districts indicated that they did not have a written plan to address Y2K issues, while twenty-seven did have such a plan. One hundred and forty districts had not calculated the financial impact of the failure to bring the technology into compliance, while sixteen districts had calculated the financial impact. Twenty-nine districts ventured a guess at the financial ramifications of non-compliance.⁴ Ninety-nine districts had not budgeted resources to address Y2K issues, while fifty-six districts had budgeted such resources. The summary section of the survey results, stated that it appeared that schools were largely unprepared for the Y2K conversion, and that significant numbers of the districts had not allocated funds to attain compliance.

⁴ 25 districts pegged the cost at \$50,000 or less

4 districts pegged the cost at \$51,000 to \$100,000

1 district pegged the cost at \$101,000-\$250,000

Plaintiff argues that based on the information defendant obtained in response to the above survey, it is clear that numerous school districts are part of this putative class and have coverage claims against defendant. However, while the survey results report several school districts estimated Y2K expenditures, those estimates were made in September or October of 1998. Plaintiff presented *no evidence indicating that the estimates reflect actual expenditures or that any of the other proposed class members sustained any damages with regard to Y2K*. The results of the September 1998 survey, standing alone, do not show that any of the proposed 400 class members suffered any damage as a result of Y2K problems, let alone that they wished to assert an insurance claim for those damages. Instead, plaintiff's arguments rely on speculation as to the size of the class, which is insufficient to establish numerosity. See *Marcial v Coronet Ins Co*, 880 F2d 954, 956 (CA 7, 1989).

“Generally speaking, factual findings are clearly erroneous if there is no evidence to support them or there is evidence to support them but this Court is left with a definite and firm conviction that a mistake has been made.” *Zine, supra* at 270, citing *Featherston v Steinhoff*, 226 Mich App 584, 588; 575 NW2d 6 (1997); *Lumley v Univ of Michigan Bd of Regents*, 215 Mich App 125, 135; 544 NW2d 692 (1996). We conclude that the trial court did not clearly err in denying plaintiff's motion for class certification because plaintiff failed to prove that the proposed class was so numerous that joinder was impracticable. Further, because plaintiff has not adequately identified potential claims or claimants, it has not shown that there are questions of law or fact common to the members of the class that predominate over questions affecting only individual claimants, that plaintiff's claims are typical of the claims or defenses of the class, that plaintiff will fairly and adequately assert and protect the interests of the class, or that a class action will be superior to other available methods of adjudication. Under the circumstances, the trial court did not err in denying plaintiff's motion for class certification.

Affirmed.

/s/ Kurtis T. Wilder
/s/ Richard Allen Griffin
/s/ Hilda R. Gage